mailto:regs.comments@federalreserve.gov

February 16, 2021
Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Ave. NW
Washington, DC 20551

RE: Regulation BB: Community Reinvestment Act, Advance Notice of Proposed Rulemaking, Docket Number R-1723 and RIN 7100-AF94

Dear Ms. Misback:

I am writing to comment on the Advance Notice of Proposed Rulemaking (ANPR) entitled Community Reinvestment Act (CRA), which was published by the Federal Reserve Board of Governors ("the Board") on October 16, 2020.

I first would like to thank the Board and its staff for its leadership to update the CRA regulations. It is my hope, and that of many others, that the issuance of this ANPR will result in a single set of regulations that can be adopted by all three bank regulators (Federal Reserve, OCC, and FDIC).

My name is Mark A. Willis. The opinions expressed here are my own. I am currently a Senior Policy Fellow at the NYU Furman Center where I work mainly on community development (including the Community Reinvestment Act), affordable housing, housing finance, and tax policy. I previously headed community development for Chase/JP Morgan Chase, initially as the founding president of the Community Development Corporation at Chase Manhattan Bank and 19 years later leaving JPMorgan Chase as executive vice president for Community Development. Among my duties during those years I had direct responsibilities for the bank's CRA activities/compliance. Building on that experience I have continued to this day to write and lecture extensively on CRA and proposals for reform. Of my writings, two publications of note are my 2009 paper ("It's the Rating, Stupid: A Banker's Perspective on the CRA") in *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*, a joint publication of the Boston and San Francisco Federal Reserve Banks (https://www.frbsf.org/community-development/files/revisiting_cra.pdf) and, "Updating CRA Geography: It's Not Just About Assessment Areas" (https://penniur.upenn.edu/uploads/media/Mark_Willis_10-1.pdf) which was published in *Housing Policy Debate* and where I directly tackled the issue of evaluating CRA performance for internet banking.

Rather than respond specifically to each of the questions in the ANPR (I leave that task to others more currently involved at the ground level), I have chosen to provide a possible framework for evaluating the CRA performance of banks that serve retail customers located beyond the geographies covered by physical branches. Before turning to that topic, though, I want to highlight an overall concern I have about preserving the criticality of qualitative judgment in evaluating the CRA performance of banks. In that regard, I appreciate the careful wording of the following objective as stated in the ANPR:

> Increase the clarity, consistency, and transparency of supervisory expectations and of standards regarding where activities are assessed, which activities are eligible for CRA purposes, and how eligible activities are evaluated and assessed, while seeking to minimize the associated data burden and to tailor collection and reporting requirements.

I am in complete accord with the desirability of enhancing “clarity, consistency, and transparency,” and note with appreciation the absence of such words as “predictability” and “certainty” that sometime are conflated with these terms. While I support enhancing clarity, consistency, and transparency as much as possible, I am concerned that those efforts can unintentionally lead to an overreliance on quantitative measures and a diminishing of the importance of qualitative judgments. The strength of the CRA has been in preserving a balance between quantitative and qualitative assessments of a bank’s CRA performance. To move too far in the direction of quantifying everything risks losing the importance of impact as a key factor for rating a bank's CRA performance.

I say this because one of the strengths of the CRA has been to pushes banks (“thumb on the scale”) to look for ways they can use their expertise to undertake activities that have incrementally beneficial impact on low- and moderate-income (LMI) people and communities—an impact beyond what would otherwise flow from their normal course of business. By not allowing CRA to become just a numbers or check-the-box game, banks have been encouraged to devote the time, attention, and resources to find ways to make safe and sound investments that improve the lives of LMI people and communities. Qualitative judgment is needed as qualitative metrics are often ill-suited for measuring this type of incremental effort and impact. So it is critical that qualitative judgments continue to receive sufficient emphasis/weight as you revise the regulations.

This does not mean that clarity cannot also be a tool to provide certainty as to what qualifies for CRA credit. In particular, I support the added certainty that the Board is offering through “a pre-approval process for community development activities focus on specific proposed transactions, or on more general categories of eligible activities.” Providing a means to clarify a projects eligibility for CRA credit will provide valuable information to banks looking to determine where to focus their finite resources. However, clarity on this point does not, and should not, by itself, guaranty a bank’s overall CRA rating.

A FRAMEWORK FOR ASSESSING THE CRA PERFORMANCE OF LARGE RETAIL BANKS IN THE INTERNET AGE

The following proposed framework for evaluating the CRA performance for large retail banks outside of their branch-based assessment areas (AAs) has benefitted from conversations with a wide range of stakeholders ranging from bankers to community groups to regulators, all of whom share the goal of strengthening the impact of CRA for LMI people and communities while eliminating unnecessary regulatory constraints.

“Modernizing” CRA based on geography of the customer

A key reason for “modernizing” the CRA is to provide more clarity about the process for evaluating CRA performance in light of the growth in internet banking. This growth has allowed banks to serve customers beyond the boundaries of the areas they can service through their publicly accessible, physical, deposit-taking branches. Even customers located within “branch-serviceable” areas (locations where going to a branch is an option) may carry out most or all of their banking through the internet or other remote means. (The term “branch-serviceable areas” covers functionally the same geography as is intended with “branch-based assessment areas” as both look to include all those customers who live/work within a reasonable distance of a branch; I would suggest that the Board give consideration to replacing “AA” terminology with “Branch-Serviceable” areas to remove any doubt that there are also additional geographies beyond branches where CRA performance also needs to be evaluated/assessed. Note: to minimize any possible confusion, this comment continues to use “AA” terminology.)

While my proposed framework continues to assess CRA performance within AAs, it also provides a framework for when and how to evaluate a bank's CRA performance outside its AAs. The logic of separately evaluating taking into account non-AA activities is straightforward. Evaluation of CRA performance should not stop at the border of a bank's branch geography. However, customers outside of branch-based assessment areas have a different relationship with their bank as they mainly, if not exclusively, have to rely on remote access, internet or otherwise, for their bank services. And correspondingly, banks have a different relationship with those customers as they lack personnel on the ground in those locations. My contribution to modernization is then to provide a framework for building into a bank's rating an evaluation of its non-AA CRA performance when a substantial amount of retail business is with customers beyond its AAs.

<u>Basic principles</u>

The creation of this framework was motivated by the following principles:

- Minimize complexity (i.e., keep it simple)
- Maximize the reliance on existing regulatory procedures/approaches (for purposes of this comment, the examples below rely on key elements of the ANPR noted below)
- Provide large retail banks with one set of rules that offers clarity, consistency, and transparency and can seamlessly accommodate changes over time as banks evolve their branch and internet business strategies
    - Avoid discontinuities other than a de minimis test for being classified as a hybrid bank.
- Allow banks to focus their non-AA community development (CD) activity according to local CD opportunities/needs and bank strategies and not be unnecessarily geographically restricted.
    - Allow for full CRA credit for CD activities in CRA/credit deserts, i.e., no geographic restrictions on CD activities to qualify for CRA credit at the institution level (incentives should be built into the regulations to proactively encourage these types of activities)
- Avoid the creation of CRA hotspots
- Evaluate retail and CD separately and, whether measuring performance inside or outside AAs, use similar metrics
    - For evaluating retail products use the comparator approach to assess the share of retail products in LMI communities and to LMI borrowers
    - For evaluating CD use a deposit-based ratio test.
- Determine final ratings by blending the AA and non-AA CRA performance ratings
- Retain Strategic Plan option for banks with unusual circumstances

<u>Elements of ANPR relied upon for purposes of this exposition</u>

The basic structure I propose for separately evaluating activities within and outside of AAs is not dependent on all of the specifics laid out in the ANPR and should be adaptable to any further modifications of the metrics/benchmarks or the process for rating AAs. For purposes of this exposition of my proposal I do assume that the following elements of the ANPR are in place:

- The separate analysis of retail and CD performance;
- Branch-based AAs but no additional AAs based on deposits or loan-production offices
- Methodology for determining AAs ratings
- AA ratings used to build state ratings
- Methodology for determining institutional level ratings retained for banks for without significant retail lending beyond their AAs;
- A CD test but no retail test for wholesale and limited purpose banks; and
- Retention of the strategic plan option.

Method for evaluation of retail lending outside branch-based AAs.

Banks that make a significant share of their home mortgage or small business loans outside their facility-based AAs should have those loans assessed in the aggregate for meeting the needs of LMI communities in the same way that loans within AAs are assessed.

- Applicability: A bank's loans in any retail lending product line (e.g., home mortgage or small business loans) made outside its facility-based AAs would be separately evaluated *in the aggregate* if they comprise at least 20 percent of the bank's total loans in that product line. No analysis of retail lending would apply for any product line if such loans outside the bank's facility-based AA comprise fewer than 20 percent of its loans within that retail product line.
- Comparators: The loans will be subjected to the same community and industry comparator tests as to geography and borrower as would be applied at the AA level for each applicable retail lending product line. (LMI determination based on local AMI data.)
- Institution-Level Benchmark (used for assessing level of performance), Two options:
    A. A single "nationwide benchmark" for each retail lending product line to be used regardless of a bank's distribution of loans across geographies outside its AAs; or
    B. "Tailored benchmarks" for each retail lending product line to reflect each bank's actual mix of markets served outside its AAs, weighted based on the number of loans in each market.

    [The Board should analyze retail lending data to determine whether to adopt the nationwide or the tailored benchmark approach. In concept, the tailored benchmark might be more accurate and fairer than the nationwide benchmark, but it could be simpler for all banks to have the same benchmark. The Board is best positioned to determine how much the variance among local markets matters and whether the benefits and drawbacks of the tailored approach are worth the additional accuracy. The Board could instead allow any bank to use the nationwide benchmark but permit a bank to develop the tailored benchmark at its option.]
- State level rating (relevant only for states where the bank has one or more AAs)
    - The state retail rating could simply be built up from the retail ratings of the one or more branch-based AAs. Qualitative consideration could be given for any LMI retail loans and services outside of AAs (within the relevant state), taking into account any performance context as appropriate.
    - Overall CRA rating would be derived as a blend of Retail and CD ratings
- Weighting of retail lending within and outside AAs would be based on the share of loans outside AAs for each applicable product line or, alternatively, on a combination of the share of a bank's loans outside AAs and the share of deposits received from outside its AAs. Accordingly, AA performance would be weighted more heavily if that is where a bank is lending, while a bank that mostly lends outside its AAs would have that lending weighted more heavily.

Method for evaluation of CD activity outside branch-based AAs.

Non-AA CD activities would be combined with AA-level CD activities at the institution level to provide a consistent standard across all retail banks and support bank CD activities regardless of geography. Qualitative credit should be used to reward activities with particularly desirable impact. Non-AA and AA CD activities are combined in evaluating CRA performance at the institution level.

- Single Institution-Level CD test: Total CD activity – both within and outside its AAs – would be measured against a bank's total domestic deposits.
    - No change in evaluation of CD performance at the AA level but banks can also get credit for additional CD activities regardless of geography, e.g., in areas of greater need.

- No specific requirement for non-AA CD activities (a bank's local CD activity would continue to be evaluated AA by AA).
- State rating (relevant only for states where the bank has one or more AAs)
  - The CD rating could simply be built up from the CD ratings of the one or more branch-based AAs. Qualitative consideration could be given for any CD activities outside of AAs, taking into account any performance context as appropriate.
  - Overall CRA rating derived as a blend of Retail and CD ratings

<u>Examples for Three Types of Banks: Branch-Based, Branchless, and Hybrid</u>

Here is how the proposed framework would work for three types of banks: those with no substantial retail lending beyond their branch-based assessment areas, those with no branches (or just a main office AA), and those with both branch-based assessment areas and substantial lending beyond those geographies for at least one product line (so-called hybrids). For exposition purposes, these examples assume the ANPR is in place. The evaluation of retail and CD are explained separately as each are rated before being combined to yield CRA ratings at the AA/metro, state, and institutional level.

A. Determination of Retail Ratings

I. Branch-based bank with no retail lending line having more than 20% of its loans outside of AAs

<u>Level</u>	<u>Methodology for Retail test</u>
AA	As per ANPR
State	Weighted average of the retail test ratings of the AAs within the state as per ANPR plus qualitative for non-AA retail activities)
Institution	As per ANPR (retail rating is a weighted average of the AA retail test ratings)

II. Branchless bank with and without a main office AA

<u>Level</u>	<u>Methodology</u>
AA	NA if no main office AA, otherwise as per ANPR
State	NA if no main office AA, otherwise as per above approach for branch-based AAs
Institution	

Without main office AA

- Comparator tests for retail lending at the institution level with benchmarks to be determined according to either the "tailored" and "non-tailored" institution-level benchmark discussion above.

With main office AA, a blend of:

- AA rating weighted based on its share of the institution's loans and/or deposits as per ANPR, and
- The non-AA retail lending rating at the institution level would be determined only for retail lines which exceed the 20% non-AA threshold using the comparator tests at the institution level with benchmarks to be determined according to either the "tailored" and "non-tailored" approaches discussed above. Additional qualitative credit would be given for any retail services not included in AA ratings. (Retail lines with more than 80% of the loans within AAs would not be subject to a non-AA retail lending test.)

III. Hybrid with mix of branch-based AAs and more than 20% of loans made outside of AAs for any of the retail lending lines (Retail lines with more than 80% of the loans within AAs would not be subject to a non-AA retail lending test)

<u>Level</u>	<u>Methodology</u>
AA	As per ANPR
State	As per ANPR (weighted average of the retail ratings of the AAs within the state)

Institution	Blend of the aggregate AA rating and the non-AA rating

- The AA level ratings would be aggregated to the institutional level as per ANPR, and
- The non-AA retail lending rating at the institution level would be determined only for retail lines which exceed the 20% non-AA threshold using the comparator tests at the institution level with benchmarks to be determined according to either the “tailored” and “non-tailored” approaches discussed above.

B. Determination of CD Ratings (assume CD services only receive qualitative consideration)

I. Branch-based bank with limited retail lending outside of AAs

Level	Methodology for Community Develop Lending and Investment Subtest
AA	As per ANPR with only qualitative consideration for CD services
State	Blend of AA CD ratings with qualitative consideration for non-AA CD activities.
Institution	Metric is ratio of bank wide CD lending and investment over total deposits

II. Branchless bank with and without a main office AA

Level	Methodology
AA	NA if no main office AA, otherwise as per ANPR metric based on local deposits
State	NA if no main office AA, otherwise as per above approach for branch-based AAs
Institution	

Without main office AA

Metric is ratio of bank wide CD lending and investment over total deposits (with qualitative consideration for CD services)

With main office AA

Metric is ratio of bank wide CD lending and investment over total deposits (with qualitative consideration for CD services)

III. Hybrid with mix of branch-based AAs and more than 20% of loans made outside of AAs for any of the retail lending lines

Level	Methodology
AA	As per ANPR
State	As per above approach for branch-based AAs
Institution	Metric is ratio of bank wide CD lending and investment over total deposits (with qualitative consideration for CD services

Thank you for your consideration of these comments on the ANPR.

Sincerely,
Mark A. Willis